The occasions are rare when a Regulator makes one stand up and applaud. The Consultation Paper put out by SEBI, seeking comments on the proposed amendments to the SEBI LODR Regulations, 2015 is one such instance. There is clarity and consistency. The hope is that it will not fail the test of continuity.

Editor

WHEN CONTEXT AND CONTENT CONVERGE

M. Damodaran
Chairperson, Excellence Enablers
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Following close on the heels of the RBI's Discussion Paper on Governance in Commercial Banks, and the first guideline based thereon, the SEBI consultative paper to review the SEBI LODR Regulations, 2015 (Regulations) comes as a breath of fresh air. In a departure from several such exercises in the past, this paper sets out the objectives with considerable clarity, and proceeds to propose changes that are consistent with the stated objectives. While this might seem commonsensical, it is not a usual practice witnessed in the regulatory scenario.

A few comments on the objectives are in order. The first objective, understandably, is to strengthen Corporate Governance practices and disclosure requirements. The second is to ease the compliance burden on listed entities. Taken together, both these objectives underscore the oft-expressed view that Regulations that ease the compliance burden, can, and does, co-exist with better Corporate Governance practices. The third objective is to maintain internal consistency within the Regulations as also to harmonise them with the provisions of the Companies Act, 2013 (the Act). The fourth objective, which is to maintain gender neutrality, is important enough to have been categorised separately, rather than to have been clubbed with the harmonisation objective.

The first two proposed changes, which are new provisions, relate to the continuity of the level of governance standards and practices, irrespective of whether the market capitalisation of the company has fallen below the prescribed threshold, or changes have been effected in the equity share capital or the net worth of such entities. This is a welcome clarificatory addition to the Regulations. It cannot be anyone's case that because of movements in the market, leading to the market cap of a company falling below a prescribed threshold, the applicable regulations and governance standards ought to be different. Similarly, changes in net worth or in equity share capital should not lead to dilution in regulatory standards in respect of the concerned company. Continuity of regulatory standards is a virtue in any regulated universe, and it should apply equally to individual regulated entities.

The third proposed change is, on the surface minor, but has significant effect. The loophole exploited by some corporate entities by keeping the parent shareholding at 50% in the subsidiary, and retaining control without being challenged by Regulation 24(5) of the Regulations, has been plugged by changing the words 'less than 50%' to 'less than or equal to 50%'.

The periodicity of, and time limits for, disclosure of events or information has been another problematic area. The existing provision is for disclosure to be made in respect of some specified events within 30 minutes of the conclusion of the Board meeting. It is entirely possible that if some price sensitive decisions, such as financial results, are taken at an early stage in the meeting, to hold back the disclosure to the Stock Exchanges till after the end of the meeting could lead to information leakages. As a responsive and responsible Regulator, SEBI has now opted for the formulation that instead of within 30 minutes of the conclusion of the Board meeting, the disclosures should be made within the timelines specified in the Schedule. This would enable companies to make disclosures of important price sensitive information within 30 minutes of approval by the Board, rather than within 30 minutes of the closure of the meeting. One unintended outcome would be multiple disclosures by the same company on the same day, but that is a small price to pay as compared to the possibility of leakage of information.

Dividend Distribution Policy (DDP) has also received attention. The present stipulation is that the top 500 listed entities based on market cap shall formulate a DDP, which shall be disclosed in the annual reports and on the websites of the companies. This is now proposed to be made mandatory for the top 1000 companies by market cap. The intention is to benefit a wider set of shareholders. This opportunity could also have been taken to examine whether the existing policies are what the Regulator intended. Some companies have in their policies, given priority to retention as opposed to payout. This is not a progressive stance, especially in present times. A review of the existing DDPs could lead to policies that are better crafted, with the interest of the shareholders not being given secondary importance.

One provision regarding easing the compliance burden on listed entities relates to the periodicity of submitting a compliance certificate, duly signed by the Compliance Officer of the listed entity and the authorised representative of the Share Transfer Agent (STA) to the Stock Exchanges. On the basis that change of RTA is not a frequent occurrence, and that any change would have to be disclosed within 7 days, the half yearly compliance certificate is proposed to be made an annual compliance certificate. While the reasoning behind the proposed change cannot be faulted, it would be preferable to stick for the time being with the 6 monthly certificate, given that there have been some significant lapses on the part of some RTAs.

Yet another change proposed is to do away with a proviso which lays down that where the dividend exceeds INR 1500, the payable at par warrants or cheques should be sent by speed post. While doing away with this proviso, SEBI has recognised that there are some investors to whom dividend is paid by means of warrants/ cheques. This would have been an opportunity to move towards complete electronic transfers, without having a few investors still opting for physical instruments, and often complaining of the non-receipt thereof. If complete dematerialisation could be mandated, there is no reason not to travel forward on that journey and to stipulate that all payments of dividends shall be by electronic means.

Yet another constructive proposal is to delete the provision that the listed entity shall publish in newspapers the notice of the meeting of the Board of Directors where financial results shall be discussed, as also statements of deviation or variation. It is now proposed that only the financial results, as specified, will be required to be published. This is a cost reduction measure, which is positive from a compliance perspective also.

The harmonisation of provisions also addresses some gaps. The term 'firm' and the term 'working days' which had not been defined earlier, are now proposed to be defined. Similarly, consequent on the amendment of the definition of 'independent director' in May, 2018, there is a consequential modification proposed to expand the requirements for transactions of relatives, and to harmonise it with the Act. However, a lower threshold for pecuniary relationships of relatives is proposed to be retained. It would have been useful to harmonise this also with the provisions of the Act.

It is not proposed in this newsletter to attempt a clause by clause analysis of the proposed changes. Suffice it to say that the proposed changes are in the right direction, and should address the objectives with which SEBI has embarked on this exercise.

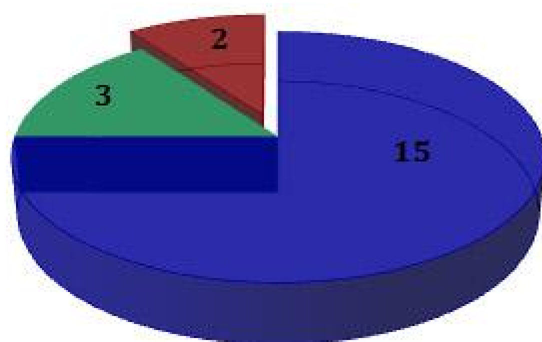
This consultative paper should sail through without much opposition or obstruction. Responsibility and responsiveness seem to be writ large in this exercise.

Excellence Enablers recently co-hosted a webinar with NSE, on Corporate Governance and Financial Regulations. This was the second of a three part series - CONVERSATIONS ON CORPORATE GOVERNANCE. For more, click here

THE STORY SO FAR...

Distribution of committee memberships among IDs in Nifty 50 cos#

Rationale: An equitable distribution of board committee memberships is essential to capture the totality and diversity of experience in the boardroom.



Cos with at least 1 ID on no committee

Cos with at least 1 ID on all 5 committees

Cos with at least 1 ID on no committee and at least 1 ID on all committees

#Nifty 50 cos except SBI, as on 31/03/2020. SBI has separate Nomination and Remuneration committees, and has been excluded.
****5 committees include AC, NRC, SRC, CSRC and RMC***
*****Source: Annual Reports of respective cos for FY 2019-20***

READERSPEAK - NOT A GOING CONCERN

Bharat Doshi, Former Non-Official Director, Central Board, RBI and Former Group CFO, M&M
"It is time to rebuild trust of the stakeholders in the objectivity of the audit process and in the institution of auditors. May be an independent body comprising auditors, corporate CFOs, Stock Exchanges and Regulators can create a framework to achieve this goal."

Nawshir Mirza, Former Senior Partner, M/s S.R Batliboi & Co.
"My concern is that as a consequence, auditors will now go entirely by the book so that every audit will take much longer and cost much more without commensurate benefit to the users of the audit opinions emerging. No doubt, it will stop a few audits from failing but the cost of that may be too great."

Milind Kulkarni, Senior Advisor and Former CFO, Tech Mahindra
"The trend of loss of audit independence is not new but what is worrying is that the instances are increasing and the mighty have also fallen."